

Alberta economic trends

June 2012

Alberta economy continues to strengthen, but global risks remain elevated

Recent economic indicators signal a solid pace of expansion in Alberta. Business output continues to trend upwards, and ongoing strength in the labour market has pushed net interprovincial migration to levels not seen since 2006 in the first quarter. However, the global economy remains unstable and oil prices have retreated, posing a risk to the Alberta economy. The InFocus uncovers the multi-dimensional issue of productivity, a key driver of long term economic prosperity.

Global Economy

All eyes on Europe

Spain is the latest EU member to land in the crosshairs of the European debt crisis. Earlier this month European leaders agreed to provide 100 billion Euros to recapitalize ailing Spanish banks, hurt by loans made during the last construction boom. Spanish 10-year government bond yields remain close to 7% reflecting continued concerns over Spain's financial stability and weakened economy. Spain now joins Greece, Portugal, and Ireland as recipients of EU bailout funds.

In Greece, pro-bailout parties were elected on June 17th and have formed a coalition

Key Indicators

All indicators seasonally adjusted unless otherwise indicated.

Indicator	Latest Month	Value	Change year-over-year (y/y)
Employment (thousands)	May	2,153	4.1%
Unemployment Rate	May	4.5%	0.9 p.p.
CPI Inflation	May	0.4%	-2.4 p.p.
Retail Sales	April	\$5.65B	+7.8%
Housing Starts (annualized)	April	31,400	+25.1%
Rigs Drilling (unadjusted)	June	139	-7.3%
Manufacturing Shipments	April	\$6.3B	+7.9%
Exports	April	\$8.4B	+21.2%

Source: Statistics Canada, CMHC. p.p.= percentage points.

majority. The election result abates concerns of an immediate Greek exit from the Eurozone. However, doubts remain over Greece's ability to achieve austerity goals.

The situation in Europe has translated into greater uncertainty and weighed on other regions of the global economy. In China, growth continues to slow, with first quarter GDP growth of 7.5% hitting the lowest in three years. Chinese authorities have already responded; the central bank has relaxed reserve requirements and lowered its benchmark interest rate this month.

South of the border, job creation is slowing. After a solid first two months of the year, US

employment growth has cooled significantly, with only 69,000 jobs added in May. On a positive note, the long struggling US housing market is finally showing some signs of improvement; housing starts are up 26% in the first five months of 2012 over last year.

World oil prices soften

Oil prices have retreated amid renewed economic uncertainty. The price of Brent crude fell below \$US100/bbl on June 1st for the first time since February 2011. WTI has fallen to the \$US80-85/bbl dollar range this month, after averaging close to \$US95/bbl in May.

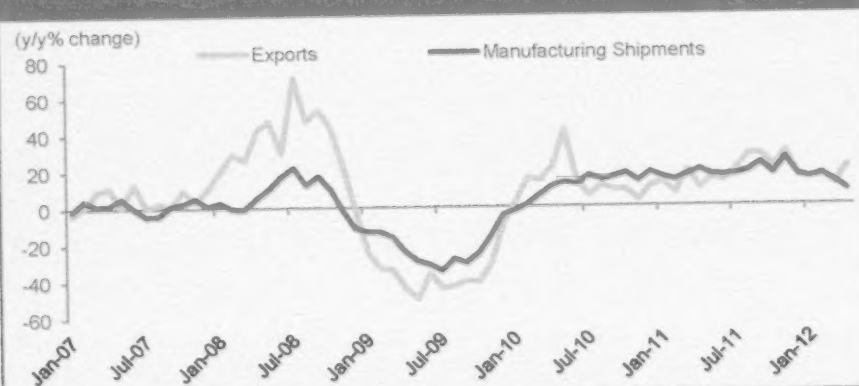
Business Sector

Business output continues to trend upward

In a weak global economic climate, Alberta's trade performance has been relatively strong. While exports slipped 4.9% in April from March, they were up 21.2% year-over-year (y/y) for the largest gain since November. Energy products, which account for almost three quarters of Alberta's total exports, were \$1.4 billion (+31%) above last April. Year-to-date, exports are up a solid 15.9% over last year, although the recent fall in oil prices will likely weigh on export growth in May and June.

In Alberta's manufacturing sector, shipments have seen strong gains over the last year. Through April, shipments are up an impressive 12.9% over the same period last year.

Chart 1: Growth in Exports and Manufacturing Shipments



Source: Statistics Canada

However, the pace of growth has been moderating. Shipments have dropped in 4 of the past 5 months and year-over-year growth has eased to 7.9% due primarily to weaker gains in refined petroleum & petrochemical shipments.

Oil and gas industry capacity utilization reaches close to a 10-year high

The Canadian oil and gas industry, which is concentrated in Alberta, reached its highest capacity utilization level in almost a decade in the first quarter. The industry was operating at 90.2% of capacity in early 2012, up 3.4 percentage points from a year ago. This utilization rate is well above the 80.7% total industry average for Canada.

The number of rigs drilling in Alberta, a more timely indicator of activity, was down 7.3% y/y in June. However, rigs drilling was still up 3.5% in the first half of 2012 over the same period last year.

Permits indicate stronger building activity

Construction activity is poised to strengthen further in Alberta according to the latest building permit data. The value of non-residential building permits jumped by 158% y/y in April. Permit data are notoriously volatile on a monthly basis, but the year-to-date increase of 10.5% provides an indication of an upward trend.

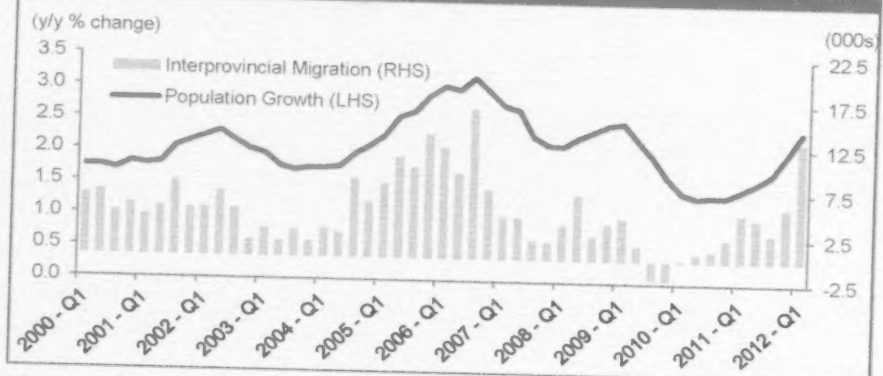
Residential permits have also jumped this year, by 22.2% year-to-date. This, combined with a rebound in housing starts, suggest that 2012 will be a stronger year for housing construction.

Household Sector

Alberta job growth leading Canada this year

Alberta's labour market has picked up markedly in the last two months after a relatively slow first quarter. In May, the province added 9,800 new positions, following a similar gain in April. May's gains were broad-based across most industries, with the majority in full-time and self-employed positions. Year-to-date, Alberta leads the country in employment growth at 3.6%. The unemployment rate dipped by 0.4 percentage points last month to 4.5%, the lowest rate since December 2008 and tied with Saskatchewan for the lowest in Canada.

Chart 2: Alberta Interprovincial Migration and Population Growth



Source: Statistics Canada

Destination Alberta. More Canadians moving to the province

Attracted by job opportunities, Alberta gained 13,396 migrants from other provinces in the first quarter of 2012, the strongest quarterly gain since 2006. Alberta welcomed residents from every province and registered the ninth straight quarter of positive net interprovincial inflows. At an estimated 3,847,119 as of April 1, 2012, Alberta's population has grown by 89,000 from the same time last year, representing a nation-leading 2.4% increase.

Alberta rental vacancy rate drops; housing starts continue to outperform last year

The influx of migrants to Alberta seems to be putting pressure on the rental market. The rental vacancy rate fell to 3.0% in April from 4.7% April 2011. In both Calgary and Edmonton, the vacancy rate dropped below 3% with Edmonton hitting a 5 year low of 2.7%. The Fort McMurray area's vacancy rate bucked the provincial trend, increasing to almost 11% from 6.4% in April 2011. Higher rents and more workers living in camps contributing to the uptick according to CMHC. The market for new homes in Alberta also continues to improve. While housing starts fell in May, they were still up 25% y/y and year-to-date have risen 47%.

Earnings continue to rise, but growth moderates

After a run-up in late 2011, Alberta earnings are now growing at a more moderate pace. Average weekly earnings grew by 2.8% (y/y) in the first quarter, well below the previous 7 quarters of 4% or greater earnings growth. Higher earnings have helped boost retail sales, which have grown by 9.5% year-to-date over last year. Big ticket purchases, including spending at auto dealers (+17.8%) and furniture stores (+11.1%), have helped drive retail sales so far in 2012.

Consumer price inflation in Alberta fell for the 7th straight month, coming in at only 0.4% in May on the back of falling energy prices and slower growth in food prices. Inflation excluding volatile food and energy prices dropped to 1.5%, indicating that core inflation pressures remain at bay. With earnings growth outpacing inflation this year, Albertans continue to see gains in real (inflation adjusted) wages.

Help Wanted

New information from Statistics Canada shows just how tight Alberta's labour market is, and how difficult it is to find workers. One indicator, the job vacancy rate, illustrates how many jobs are vacant for every job required (vacant or filled). Alberta's reading of 3.5% was almost double the national average of 1.8%.

Another new measure depicts the number of unemployed for every vacant position. Again the Alberta labour market leads Canada with only 1.8 unemployed workers for every job vacancy, compared to 5.8 on average in Canada. Both new indicators reflect the strong employment growth and the availability of jobs in the Alberta economy.

Productivity In Context

Labour productivity is linked to economic prosperity and living standards. Unfortunately, Canada has failed to keep up with its peers in this area. This InFocus looks at drivers of productivity growth and discuss Alberta's productivity results in a national context

Why productivity matters

Labour productivity, the economic value (GDP) generated per hour worked, drives living standards in the long run. While labour supply is limited, labour productivity can continue to increase through efficiency gains and by producing new and improved goods and services. Canada's aging population means that workers must become more productive to support a higher standard of living for themselves and their older, retired peers.

Canada's productivity growth has lagged behind

Canada has not kept pace with its peers when it comes to improvements in productivity. Over the last ten years, Canada's labour productivity advanced at an average pace of 0.9% a year, under half of the US increase and roughly 60% of the G7 average rate (Chart 1). As a result of Canada's low growth rate, the gap between US and Canadian labour productivity has widened from approximately 10% in 1980 to nearly 25% in 2011, according to the Center for the Study of Living Standards (CSLS).

Many possible causes of Canada's underperformance

There is no single explanation why Canada's productivity growth has lagged. Productivity is a multi-dimensional issue, and unravelling the potential causes is complex. However, a number of explanations have been suggested by researchers, including lower levels of business innovation, certain skills gaps, and weaker investment in research and development (R&D) and machinery and equipment (M&E).

Business innovation involves finding better ways to extract value from capital and labour. Research indicates that multi factor productivity (MFP), a rough proxy for business innovation, is the principal reason for Canada's weaker productivity growth.¹

Another key driver of productivity growth is the adoption of new technologies. Investment in M&E is highly correlated with productivity growth, particularly investment in information and communication technologies. Since the 1970s, Canada's investment in M&E as a share of GDP has remained among the lowest of advanced countries. One estimate suggests that the M&E intensity gap accounts for roughly 20% of the labour productivity gap between Canada and the United States.²

Though highly educated, Canadian workers fall behind the US on some measures, including share of the workforce with a university degree and the education level of managers.³

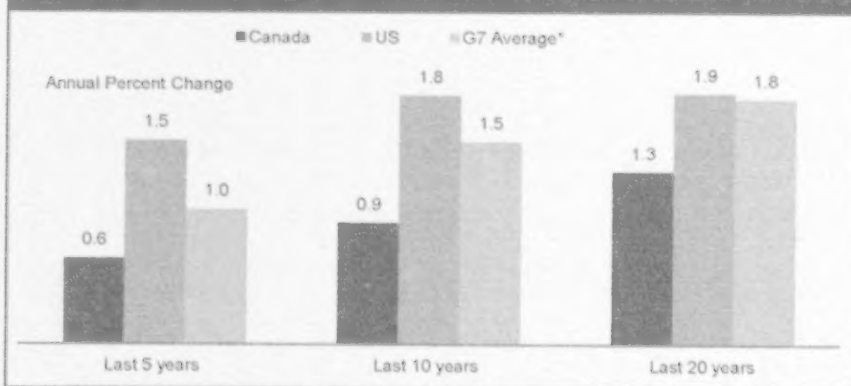
While technology can be adopted, some innovations must also be developed at home to address Canada's unique business challenges. Research and development (R&D) leads to new and improved business processes and products, yet Canada's business sector continues to lag the US and many other advanced countries in R&D spending (as a share of GDP).

Weak productivity growth experienced by many provinces

Over the last ten years, nearly all provinces have seen fairly tepid gains in labour productivity. Newfoundland and Labrador is the only province to record a stronger growth rate in labour productivity than the US since 2001. In Alberta, productivity grew by a modest 0.5% a year from 2001 to 2011, compared to 0.9% nationally.

Developments in the oil and gas sector help explain Alberta's overall productivity growth performance, including declines in conventional oil and gas productivity and the shift from conventional to non-conventional oil sands production. Over the last decade, there have been large amounts of capital and labour used for exploration and development in the oil sands, but with production not yet fully materializing. As more production comes on stream, the sector's productivity growth will likely improve.

Chart 1: International Comparison of Labour Productivity Growth



Source: Statistics Canada, CSLS and OECD

* G7 Average up to 2010 due to lack of data, while Canada and US up to 2011

Note: Last 5 years is 2006-2011, 10 years is 2001-2011, and 20 years is 1991-2011.

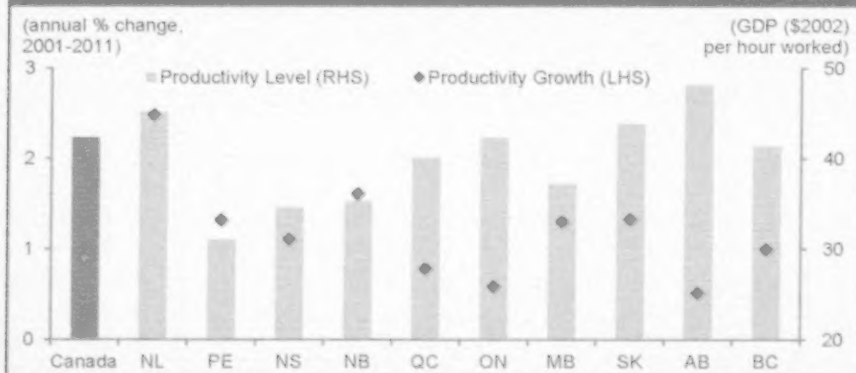
¹ Council of Canadian Academies (2009) "Innovation and Business Strategy: Why Canada Falls Short." Ottawa.

² Rao, Tang and Wang (2008) "What Explains the Canada-US Labour Productivity Gap?" Canadian Public Policy, Vol. 34, No. 2, pp. 163-192

³ Institute for Competitiveness and Prosperity (2011) "Canada's Innovation Imperative", Report on Canada, June

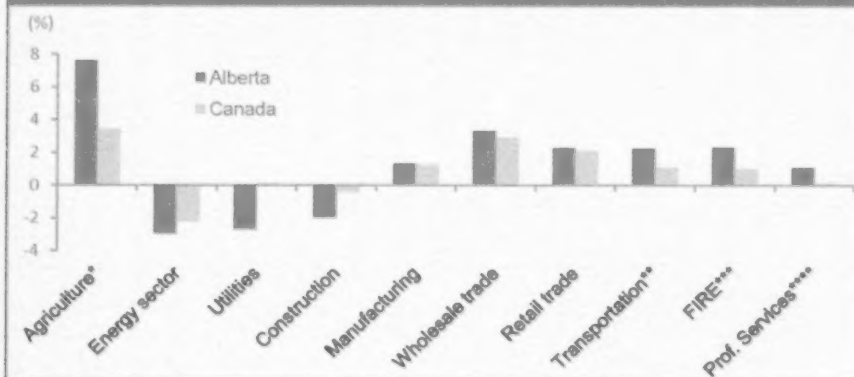
Outside the energy sector, Alberta's productivity growth fares much better, according to a recent CD Howe Institute study.⁴ The study examined productivity growth within and outside the natural resource sector for all the provinces. It found that Alberta's labour productivity growth excluding natural resource extraction was the strongest of all provinces for the periods 1985-2009 and 2000-2009. Chart 3 shows that Alberta has outpaced the national average over the last ten years across a range of industries in the service sector, and in the agriculture, forestry, fishing & hunting sector.

Chart 2: Labour Productivity by Province



Source: Statistics Canada

Chart 3: Labour Productivity Growth by Industry: 2001-2011 Annual Percent Change



Source: Statistics Canada

* Agriculture, forestry, fishing and hunting

** Transportation and warehousing

*** Finance, insurance, real estate, rental and leasing

**** Professional, scientific and technical services

⁴ Coulombe, S. (2011) "Lagging Behind: Productivity and the Good Fortune of Canadian Provinces." C.D. Howe Institute Commentary 331, June.

Alberta continues to have highest level of Labour productivity

Labour productivity levels continue to vary widely across provinces, a pattern that has persisted for many years. Alberta continues to have the most productive workforce among the provinces, a position it has held at least since 1985.⁴ Alberta's high productivity levels are in large part due to high levels of capital investment per worker. Newfoundland and Labrador and Saskatchewan are Canada's next most productive provinces, also driven by higher capital intensities in their resource extraction sectors. The lower productivity provinces are concentrated in the three maritime provinces and Manitoba.

In all, Canada's productivity growth has been relatively modest in recent years, reflecting weak gains across nearly all provinces. There is no "magic bullet" solution to boosting productivity. Employing and training skilled workers, investing in new technology, expanding to new markets, developing new products and services and improving processes are just some of the ways. Regardless of the source, a long run improvement in productivity will help support higher living standards, especially in the face of an aging population.

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